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NO. 314

IN THE

Supreme Court of the United States

OCTOBER TERM, 1938.

WICHITA ROYALTY COMPANY, ET AL, *Petitioners.*

versus

CITY NATIONAL BANK OF WICHITA FALLS, ET AL,
Respondents.

BRIEF OF PETITIONERS

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RAILEY—WICHITA FALLS

INDEX

Page

Subject Index

Citations of Opinions 1- 2

Jurisdiction 2

Statement of the Case 3-11

Specification of Errors 11-12

Summary of Argument 12

Argument:

Point 1—The Court of Civil Appeals was bound by the law of the case as promulgated by the State Supreme Court prior to removal 12-15

Point 2—The governing State law, binding upon the Circuit Court of Appeals, is set forth by the State Court in its decision of this case, without variance by any ot er State decision 15-23

Appendix 24-32

Table of Statutes and Rules Cited

Judicial Code, Sec. 240 (a) U. S. C. A. 347 2

Equity Rule 70½ 12

Table of Cases Cited

City National Bank of Wichita Falls, Texas v. Wichita Royalty Company et al, (D. C. N. D. Tex.) 18 Fed. Sup. 795 ..... 2, 5, 6

Erie Ry. Co. v. Tompkins, 82 Law Ed. Adv. Ops. 787 ..... 11, 15, 16, 23

Hill v. Wiley, 3 N. E. (2d) 1015 18

Inter State Circuit, Inc., Texas Consolidated Theatres, Inc., Karl Hoblitzelle et al v. United States of America. 82 Law Ed. Adv. Ops. 772 12

Messinger v. Anderson, 225 U. S. 436 15

Quanah A. & P. Ry. Co. v. Wichita State Bank and Trust Company, 127 Tex. 407; 93 S. W. (2d) 701 ..... 14, 16, 17, 19, 20

Page

Robbins v. Passaic National Bank, 109 N. J. L. 250, 82 A. L. R. 1368 22

Ruhlin v. New York Life Insurance Company, 82 Law Ed. Adv. Ops. 823 ..... 11, 16, 23

Steere v. Stockyards National Bank, 113 Tex. 287; 256 S. W. 586, 258 S. W. 1042 7

United State Fidelity and Guaranty Company v. Adoue & Lobit, 104 Tex. 379; 137 S. W. 648; 138 S. W. 383 19

Waialua Agriculture Co. Ltd. v. Christian, 83 Law Ed. Adv. Ops. 42 15

Wichita Royalty Company et al v. City National Bank, 127 Tex. 158; 89 S. W. (2d) 394; 93 S. W. (2d) 143 ..... 1, 3, 4, 8, 9, 10, 11, 14, 17, 18, 20, 21

Wichita Royalty Company et al v. City National Bank of Wichita Falls, et al (C. C. A.) 95 Fed. (2d) 671; 97 Fed. (2d) 249 ..... 2, 10, 11, 16, 23

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BRIEF OF PETITIONERS

I

CITATION OF OPINIONS

This case was first tried in the State Courts of Texas. Wichita Royalty Company, et al vs. City National Bank, et al. (R. 1884-1912) 127 Tex. 158; 89 S. W. (2d) 394; on rehearing, 93 S. W. (2d) 143.

Thereafter new parties were made and the case was removed to the United States District Court for the Northern District of Texas, Wichita Falls Division. (R. 88-115.) Motions to remand were severally denied. (R.

126-166.) District Judge William H. Atwell filed the Trial Court's opinion on April 9, 1937, appearing at page 1922 of the Record. It is reported in 18 Fed. Sup. 795.

The original opinion of the Circuit Court of Appeals for the Fifth Circuit (Circuit Judges Sibley and Holmes, and District Judge Mize, opinion by Judge Sibley) was filed March 23, 1938, appears at page 2069 et seq. of the Record, and is reported in 95 Fed. (2d) 671. An original Petition for Rehearing was filed April 11, 1938. (R. 2083.) It was denied by Order dated April 18, 1938. (R. 2085.) A Second Motion for Rehearing was filed May 23, 1938, under Petition for Leave to File. (R. 2087, et seq.) The Motion was entertained by the Court with opinion denying rehearing by Judge Sibley, filed June 10, 1938, and appears at pages 2092, et seq. of the Record. It is reported in 97 Fed. (2d) 249.

II

JURISDICTION

1. The jurisdiction of this Court is sustained under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925; 28 U. S. C. A. Section 347.

2. The judgment of the Circuit Court of Appeals was rendered on March 23, 1938. (R. 2081.) Petitioners' Second Motion for Rehearing was entertained by the Court, (R. 2089), and overruled with written opinion filed June 10, 1938. (R. 2092, 2094.)

3. Petition for Certiorari was filed in this Court on August 30, 1938, was granted October 17, 1938, and is No. 314, October Term, 1938.

III

STATEMENT OF THE CASE

This case originated in the State Courts. The Supreme Court of Texas fixed and determined the applicable law, and remanded it for entry of judgment in accordance therewith. Wichita Royalty Company v. City National Bank, 127 Tex. 158; 89 S. W. (2d) 394. The case now involves all that was involved in the State Courts. It now goes behind October, 1925, where it began in the original suit.

Wichita Royalty Company is a joint stock association, operating under a written and recorded Declaration of Trust, limiting the powers of the Trustee to deal only in the purchase and sale of oil and gas royalties and other oil and gas properties. (R. p. 355.)

Wichita Royalty Company, herein called the Trust, denied liability on the notes sued on in the State Courts in 1930, by the City National Bank of Wichita Falls, herein called the old Bank. The Trust filed a cross-action against the old Bank and impleaded the Bank's president, Harrell, suing for a $84,587.23 deposit balance with the old Bank, and seeking to recover its losses from the old Bank and Harrell because of their participation with one Peckham, the Trust's former Trustee, in breaches of trust. It was alleged that distinctly marked Trust funds were transferred without authority from the Trust account with the old Bank to the personal account of the drawing Trustee, whence they were distributed in part to pay the Bank the Trustee's personal debt, in part to pay the Bank's president, Harrell, that which the Trustee

personally owed him, and in part for the Trustee's personal use. A great number of the checks were payable to the order of the old Bank. Peckham, the former Trustee, died and the Substitute Trustee repudiated the former Trustee's alleged conveyances to his Trust, and tendered all properties so involved in the dual dealings by the old Trustee subsequent to October, 1925. (R. pp. 1183, et seq.)

The case was decided by the Supreme Court of Texas and remanded for a determination of the exact amount shown to be due in an accounting, liability being held to apply as a matter of law from the first time that the old Bank received a part of the Trust funds in payment of the Trustee's personal debt to it. The Court expressly held that the Substitute Trustee was within his rights in repudiating all transactions in which the former Trustee dealt with the subject matter of his Trust. The Court likewise held that limitations did not apply. It held that the tenders which the Trustee had made were good. And it held that the old Bank was liable for all funds transferred from and after its receipt of any part of the transferred funds. It likewise held that Harrell was similarly liable, receiving notice early in 1926, and being liable thereafter in all transactions in which Harrell was interested, notably in Marlborough Addition. The case was remanded to the Trial Court with instructions to apply the law thus determined. Wichita Royalty Co. v. City National Bank, 127 Tex. 158; 89 S. W. (2d) 394.

The old Bank became insolvent. (R. p. 446.) The Directors of the old Bank organized the new Bank, City National Bank in Wichita Falls, which new Bank took

over the assets and assumed the record liabilities of the old Bank. (R. p. 613.)

The Trust then amended, suing the old Bank and Harrell as before, setting up an account with its former Trustee during the entire period of his Trusteeship. It alleged that the old Bank had received transferred funds on Peckham's personal debt prior to October, 1925, as well as pleading subsequent benefits as pleaded in the State Courts. (R. pp. 33, et seq.)

In addition to its suit against the old Bank and J. T. Harrell, the Trust extended its suit to include the new Bank and the Directors of the old Bank, upon the averment that the old Bank was insolvent and its assets were taken over by the new Bank, seeking to charge the new Bank upon its assumption and as Trustee of the assets of the old, and seeking to hold the Directors of the old Bank for their action in transferring the assets of the old to the new Bank. (R. pp. 33, et seq.) The liability of the new parties, therefore, was derivate from and dependent upon liability of the old Bank.

The Federal District Court found as a fact that the old Bank had received and was liable for $2,550.00. The item should be $2,567.75, and was an overdraft dated January 11, 1926. (R. p. 582.) This was practically the beginning of the suit in the State Court. Likewise, the Court found that, "there was a direct benefit to the Bank out of the $25,000.00 loan to the Trust," in March, 1926, to such an extent that the Bank might not recover upon the note given in renewal of the loan. The Court further found benefits totaling $4,357.11 of Trust funds received by the Bank in payment of the Trustee's personal debt

to it. City National Bank v. Wichita Royalty Company, 18 Fed. Sup. 795-798. The amendment set up transactions prior to October, 1925, and the receipt of benefits by the Bank at various times, being useful as notice to the Bank of Peckham's infidelity. (R. pp. 33, et seq.) As will be detailed with record cited in the Appendix hereto attached, $4,827.71 of funds transferred from the Trust account to Peckham's account and then to Harrell's account was paid to the Bank on Harrell's debt; $5,601.48 of funds transferred from the Trust account to G. W. Peckham's personal account and therefrom paid to W. H. Peckham for a Marlborough interest was paid to the Bank upon the personal indebtedness of W. H. Peckham; and of the $15,000.00 and $25,000.00 loans which Harrell made for the bank to Peckham for the Trust, in 1926, Harrell personally received with Basham $24,611.02. Harrell, an active officer of the Bank, made each of the 1926 loans to Peckham, Trustee of the Wichita Royalty Company. (R. p. 1104.) Harrell testified that, "frequently when loans are made by the Bank of $15,000.00 or $25,000.00, the lending banker inquires the purpose for which the proceeds of the loan are going to be used." (R. p. 1295.)

Peckham had a deposit and liability account with the Bank. (R. pp. 578-610;1050-1083.) The Trust likewise had a liability and deposit account with the Bank. (R. pp. 969-1050; 884-886, 895.) During his Trusteeship, Peckham transferred $198,882.76 of the plainly marked Trust account funds to his personal account. (R. pp. 1700; 1801-1812.)

The Supreme Court of Texas in this case, citing

Steere v. Stock Yards National Bank, 113 Tex. 287; 256 S. W. 586; 258 S. W. 1042, held that:

> "Under a rule as old as the law itself, the entire deposit will be treated as Trust funds except so far as the Bank might, upon inquiry, be able to distinguish the Trust funds in said deposit from those therein belonging to Graves personally."

The Bank sought to discharge its burden to account for moneys received by Peckham from the Trust by showing book entries and/or conveyances from Peckham as an individual to himself as Trustee, all without the prior consent or subsequent knowledge of the stockholders. (R. pp. 277 et seq.)

$58,019.44 was the total of Trust checks made payable to the old Bank's order during and subsequent to March, 1926, that were reflected upon the Trust books to be in payment for one-half interest in and improvements of Marlborough addition. (R. pp. 1660, 1478, 1487-88.) Marlborough was not an oil undertaking, but a private venture which Peckham and Harrell operated, Peckham conveying the same to Texas Investment Company, where title stood at Peckham's death. (R. p. 1280.) Peckham executed a deed and handed it to the Trust's bookkeeper with a letter stating that Harrell was unwilling to be associated with the stock company, but was willing to be a partner with Peckham as an individual. (R. p. 785.) Peckham told the bookkeeper to let no one see the deed. (R. pp. 693, 739.) It was never recorded. (R. pp. 693, 733, 736-37.) The Supreme Court of Texas held that Marlborough was not a proper account for the Trustee's use of said Trust funds, and that the Substitute Trustee's

tender was good. Wichita Royalty Co. v. City National Bank, 127 Tex. 158; 89 S. W. (2d) 394.

$15,250.00 was to apply, but did not apply, upon the Trust's note payable to the bank. (R. p. 807.)

$19,828.67 was wholly unaccounted for. (R. p. 807.)

$15,140.78 was the amount of Trust funds transferred which the Bank defended by showing certain royalty interests which Peckham was supposed to have conveyed to himself as Trustee, and which the Substitute Trustee repudiated and tendered in the State Court, which repudiations and tenders the Supreme Court of Texas held good. Wichita Royalty Co. v. City National Bank, 127 Tex. 158; 93 S. W. (2d) 394. The $15,140.78 total is made up as follows: $5,000.00, defended against by the Bank by book entries in the Trust records showing the Trust's acquisition of the Anderson royalty with an affirmative showing that neither Peckham nor the Trust ever had title to the interests; $3,000.00, defended against by the Bank by book entries in the Trust records showing the Trust's acquisition of Polk royalty with an affirmative showing that neither Peckham nor the Trust ever had title to the interest; $1,920.00 was defended against by showing that the deed to the Hartley royalty with draft attached on Peckham was paid by the Bank on Trust check payable to the Bank's order; $160.00 was defended against by the Bank's showing Peckham's sale to the Trust of an Ellis County lease shown to have terminated before this suit arose; $2,500.00 was defended against by the Bank by the showing of Peckham's conveyance to the Trust of the Callahan Royalty. From these properties the Trust received no income. $2,560.78 was de-

fended against by the Bank by book entries showing the Trust's ownership of Porter Ranch, which stood in the name of Peckham, Harrell and others, was never conveyed to the Trust, with the Trust receiving $227.48 revenue therefrom before the State Court suit, in which the item was repudiated with tenders made. (R. pp. 1670-1675.) This $15,140.78 was involved in the suit in the State court with repudiations and tenders made, and the Supreme Court of Texas held the repudiations and tenders valid. Wichita Royalty Co. v. City National Bank, 127 Tex. 158; 89 S. W. (2d) 394.

The $58,019.44 Marlborough checks, $15,250.00 note checks, the $15,140.78 royalty checks, and the $19,828.67 that was unaccounted for represent the Trust's losses that were involved in the State Court prior to a decision by the Supreme Court of Texas. The difference between $198,882.76 that was transferred from the plainly marked Trust account to the personal account of Peckham, and $108,238.89 that was involved in the case at the time of its decision by the Supreme Court of Texas is the amount which the Trust amended to include after the decision of the Supreme Court of Texas, including $31,500.00 for salary after the Trustee began his peculations.

The royalty interests which Peckham caused Trust books to show were transferred to the Trust were not shown by the books to come from or through Peckham. (R. pp. 719-730.) Some of these royalties were never conveyed to the Trust. (R. pp. 725-788.) The stockholders were never advised of Peckham's personal interest in any transaction. (R. p. 791.) Appropriate tenders were made by the Trust, and an accounting sought. (R. pp. 191-231.)

The Supreme Court of Texas held that such was not a proper account for the use of Trust funds, and that the tenders were proper. Wichita Royalty Co. v. City National Bank, 127 Tex. 158; 89 S. W. (2d) 394.

The Circuit Court of Appeals for the Fifth Circuit remanded the case because of the Trial Court's failure to find facts. Wichita Royalty Co. v. City National Bank, 95 Fed. (2d) 671. In remanding the case the Court expressly decided the law to be different from the law as decided by the Supreme Court of Texas, its holding being: "We proceed to set forth our views especially on points not in harmony with those expressed by the Supreme Court of Texas." Wichita Royalty Co. v. City National Bank, 95 Fed. (2d) 671, 675.

The Circuit Court held the old Bank and Harrell not to be liable as a matter of law from and after the first benefit, being in direct conflict with the holding of the Supreme Court of Texas in the same case. It likewise held that the purchases by the Truustee from himself were not void but voidable, that the Bank could not question them, and that "only knowledge of a most barefaced fraud would have justified the bank in refusing to honor a check drawn to Peckham in payment of such property," whereas, the Supreme Court of Texas held the Bank to be liable for all transfers after the first benefit and that it was not a defense for the Bank to show the sale of properties from Peckham to his Trust which the Substitute Trustee had repudiated and tendered. The Circuit Court of Appeals further held that the Marlborough transaction, though not within the scope of the powers entrusted to the Trustee, might under extreme circumstances be held to be binding upon the Trust, if the Sub-

stitute Trustee accepted a valid title to minimize his loss, whereas, the Supreme Court of Texas had expressly held the Marlborough transactions not to be binding upon the Trust and the Substitute Trustee's repudiation and tender thereof to be proper. The Circuit Court reserved the right to pass upon the question of limitation, while the Supreme Court of Texas expressly held that limitation did not apply. Wichita Royalty Co. v. City National Bank, 95 Fed. (2d) 671; 127 Tex. 158; 89 S. W. (2d) 394.

After the First Motion for Rehearing was filed this Court decided *Erie Ry. Co. v. Tompkins*, 82 Law Ed. Adv. Ops. 787; *Ruhlin v. New York Life Ins. Co.*, 82 Law Ed. Adv. Ops. 823, and kindred cases. The Trust then filed a Second Motion for Rehearing asking the Court to modify its opinion by declaring the law as pronounced by the Supreme Court of Texas in this same case to be the law of the case. (R. pp. 2087, et seq.) The Second Motion was carefully considered by the Circuit Court of Appeals and overruled. (R. pp. 2092, et seq.) 97 Fed. (2d) 249. Seasonably and in proper time and manner the Trust applied for and was granted a Writ of Certiorari.

IV

SPECIFICATION OF ERRORS

1. The Circuit Court of Appeals erred in holding that it was not required to follow and apply the State law as announced by the highest Court of Texas in this case.

2. The Circuit Court of Appeals erred in holding that despite the determination by the Supreme Court of Texas of the law to be applied in this case, the Circuit Court of

Appeals was free to declare the State law by inference from a State decision rendered contemporaneously with the decision of the State Court in the case at bar and involving different facts and legal principles.

V

SUMMARY OF ARGUMENT

1. The Circuit Court of Appeals was bound by the law of the case as promulgated by the State Supreme Court prior to removal.

2. The governing State law, binding upon the Circuit Court of Appeals, is set forth by the State Court in its decision of this case, without variance by any other State decision.

VI

ARGUMENT

1. The Circuit Court of Appeals was bound by the law of the case as promulgated by the State Supreme Court prior to removal.

Petitioners do not complain at the Circuit Court's reversal of the judgment for failure of the District Court to find the facts specially. This Court has required a strict adherence to Equity Rule 70½. *Inter State Circuit, Inc., Texas Consolidated Theatres, Inc., Karl Hoblitzelle, et al v. United States of America*, 82 Law Ed. Adv. Ops. 772.

The Circuit Court of Appeals quite properly coupled the remand for fact findings with a pronouncement of the law by which the District Court should be governed. Petitioners' complaint arises from the Court's departure

from the State Court's decision to lay down with finality rules not in harmony therewith.

In their contention that the removal of this cause carried with it as the "law of the case" the decision of the Supreme Court of Texas, Petitioners rely on *Williams v. Conger*, 125 U. S. 397. As here, that case was instituted in a District Court of Texas and appealed to the Supreme Court of Texas where it was reversed and remanded for another trial, with the holding that a power of attorney offered by one of the parties was admissible as an ancient instrument. Thereafter the case was removed to the Circuit Court for the Northern District of Texas. On appeal, this Honorable Court decided that the power of attorney was properly admitted and that in any event this Court was bound by what had been decided on the question by the Supreme Court of Texas. The following is from the opinion of Mr. Justice Bradley:

> "But there is another reason why it is proper that we should so hold. The case was once before the Supreme Court of Texas on an appeal taken to set aside the verdict rendered on a former trial; and that Court held, under the same evidence used at the trial in the Circuit Court, that the document was admissible in evidence as an ancient one. If the action had originally been brought in the Circuit Court upon proper jurisdictional grounds, and had been tried as it was in the State Court, and if, on a Writ of Error from this Court we had decided as the Supreme Court of Texas did,—we should have felt bound by our first decision. We would not have allowed it to be questioned. Clark v. Keith, 106 U. S. 464 (27:302). The present case is in exactly the same category. The removal of the cause from the State Court does not

put us in the position of a Court of review over the Supreme Court of Texas. When it acted, it was the highest Court that could act in the cause, and stood in precisely the same position that we stand now. Its action must be accepted by us as that of a Court having plenary and final jurisdiction."

The Circuit Court of Appeals sought to distinguish the Conger decision on the ground of its being a land case in which the State decisions had peculiar weight and because the particular State Court's decision was but used to support this Court's ruling on the question. The quoted language is too definite and unqualified to admit of such limited import.

It is argued by the Circuit Court of Appeals that because the Texas Supreme Court was competent to reverse its decision and redeclare the governing law, its successor Appellate tribunal might exercise the same prerogative. That argument can not stand against this Court's authoritative commitment to the proposition that the removal of the cause does not put the Federal Appellate Court in the position of a Court of review over the Supreme Court of Texas. Any supposition that the Texas Court might shift its position on the questions involved would not be compatible with the exhaustive consideration given the case, both on original hearing and on rehearing. Wichita Royalty Co. v. City National Bank of Wichita Falls, et al, 127 Tex. 158; 89 S. W. (2d) 394; on rehearing, 127 Tex. 158; 93 S. W. (2d) 143. The finality of the decision is emphasized in the approval given it by the same Court in the contemporaneous case of *Quanah A. & P. Ry. Co. v. Wichita State Bank and Trust Co.*, 127 Tex. 407; 93 S. W. (2d) 701, p. 709.

In rejecting the "law of the case," the Circuit Court of Appeals assumes the power to "correct what may be clearly wrong." (R. p. 2074.) Even if it be granted that the "law of the case" does not completely bar a re-examination of the questions decided, it must be evident that the Circuit Court of Appeals wholly failed to give to the State Court's decision "the great consideration always due the decision of the highest Court of the State where the litigation arose, and always accorded to the decisions of that eminent Court." (R. p. 2074.) The obviously careful and extensive deliberation devoted to the case by the Supreme Court of Texas, and the division in the authorities recognized by both that Court and the Circuit Court of Appeals, must surely preserve the State Court's decision from the fate of being pronounced "clearly wrong." *Waialua Agr. Co., Ltd. v. Christian*, 83 Law Ed. Adv. Ops. 42. Yet the Circuit Court of Appeals in effect reached that result and thereby undid in large measure what had been accomplished by some four years of litigation in the Courts of Texas.

2. The governing State law, binding upon the Circuit Court of Appeals, is set forth by the State Court in its decision of this case, without variance by any other State decision.

Even if it is conceded that the "law of the case" expresses a rule of practice, (*Messinger v. Anderson*, 225 U. S. 436) permitting the extraordinary action of the Circuit Court of Appeals, that Court's refusal to follow the opinion of the State Supreme Court can not be reconciled with the recent decisions of this Court in *Erie Ry. Co. v. Tompkins*, 82 Law Ed. Adv. Ops. 787, and *Ruhlin*,

et al v. New York Life Ins. Co., 82 Law Ed. Adv. Ops. 823. The original opinion of the Circuit Court of Appeals treats the opinion by the Supreme Court of Texas as representing the applicable State law, but fails to accept its guidance. Petitioners' Second Motion for Rehearing invoked the rule of *Erie Ry. Co. v. Tompkins, supra*, (R. p. 2091.) This Court decided that case after the Circuit Court's original opinion had been handed down and just prior to the filing of the Second Motion for Rehearing.

Faced with this situation, the Circuit Court of Appeals professed on rehearing to follow the law of Texas, not as expressed by the Supreme Court of Texas in this case, but as the Supreme Court of Texas might conceivably express it if another opportunity were given it. This anomalous view is grounded on the conclusion that the Texas Court has "since done" that which is in effect contrary to its decision in this case. (R. p. 2093.) 97 Fed. (2d) 249, at p. 250. The Texas Court's disposition of *Quanah A. & P. Ry. Co. v. Wichita State Bank and Trust Company, supra*, is treated as later in time and controlling of the question involved.

The mistake as to the priority in time of the decision in the case at bar is manifest from the original opinion of the Circuit Court of Appeals, where a particular point is made of the fact that *Quanah A. & P. Ry. Co.* case was argued and decided with the present case. Wichita Royalty Co. v. City National Bank of Wichita Falls, 95 Fed. (2d) 675, Footnote 2. While the original opinion of the *Quanah A. & P. Ry. Co.* case was withdrawn and a different result reached, the final opinion was delivered on the same day that the opinion on rehearing was delivered in

this case. 127 Tex. 158; 93 S. W. (2d) 143; 127 Tex. 407; 93 S. W. (2d) 701. From the fact that the two decisions were contemporaneous, it must inescapably follow that both were designed to retain their full force and effect.

There is no conflict between the two cases and none can be inferred. The present case involved a direct participation by the old Bank, the City National Bank of Wichita Falls, in Trustee Peckham's wrongful handling of funds. The District Court, while making no formal fact findings on many matters involved, did find that the Bank received a payment of $4,357.11 on the Trustee's personal indebtedness from Trust funds transferred to the personal account of the Trustee. (R. p. 1928.) 18 Fed. Sup. 798. As shown above, the Bank received other benefits. The item of $2,550.00 found to have been so paid to the Bank, was received on January 11, 1926. (R. p. 582.) The evidence clearly sustains this finding. (R. p. 582.) The Marlborough transaction, involving more than $58,-000.00, and the other transfers and disbursements complained of in the suit as originally instituted, and carried forward on removal to the Federal Court, took place after January 11, 1926. The Supreme Court of Texas bottomed the liability of the Bank on the constructive notice visited upon it by these payments. It could not thereafter assume that the Trustee would properly use and account for other Trust funds commingled with his own in the personal account. Hence, the Bank, having notice of the wrongful application of the Trust money to the Trustee's personal indebtedness, was required thereafter to supervise the account for the purpose of preventing a subsequent misuse of Trust moneys irregularly transferred to the personal account. Failing in that duty, the Bank was liable for

the aggregate amount of Trust funds thereafter withdrawn and applied to unauthorized purposes. Included in such unauthorized purposes was the investment in Marlborough Addition, a suburban real estate venture, wholly unconnected with the business of the Trust.

The respondent Harrell's liability was also made to proceed from the knowledge he gained through his receipt of Trust money from the commingled account in January and February, 1926, in payment of the Trustee's personal obligations to Harrell and others. Thenceforward, he had constructive notice of Peckham's misapplication of funds in those transactions wherein Peckham and Harrell were jointly cooncerned. 127 Tex. 158; 89 S. W. (2d) 394, 407. Furthermore, Harrell likewise received the benefit of Marlborough checks and is liable therefor. *Hill v. Wiley*, 3 N. E. (2d) 1015, 1018, holding:

> "It is established law in this commonwealth 'that where a trustee of several estates steals money from one, with which to pay the debts of another, the latter, having been unjustly enriched at the expense of the former, may be required in equity to make restitution.' Bremer v. Williams, 210 Mass. 256, 257, 96 N. E. 687, 688; Newell v. Hadley, 206 Mass. 335, 92 N. E. 507, 29 L. R. A. (ns) 908; Fitcher v. Griffiths, 216 Mass. 174, 103 N. E. 471; Ricker v. Ricker, 248 Mass. 549, 143 N. E. 539."

The Texas Court further held that the succeeding Trustee was within his rights in repudiating all transactions wherein the defaulting Trustee personally sold property to his Trust and that moneys thus withdrawn from the commingled account would not be credited against the Bank's liability. The Court held that the unauthorized

acts of the succeeding Trustee, unknown to the stockholders, could not constitute a ratification and that the Statute of Limitation was not effectual to bar recovery.

A comparison of these holdings with the single proposition laid down in the case of *Quanah A. & P. Ry. Co. v. Wichita State Bank & Trust Co., supra*, conclusively demonstrates that the one case did not encroach in any degree upon the other. In the *Quanah A. & P. Ry. Co.* case there was but one account in the Bank, the individual account of the offending corporate officer. From time to time he tendered bills of exchange payable to himself (Hawkins) as Treasurer of the Quanah A. & P. Ry. Co., endorsed by him in such capacity, and credited by the Bank directly to his personal account. There was never any payment to the Bank, none of the checks were payable to the Bank, no transfers from a fiduciary account to a personal account in the same bank were involved, and the Bank had no knowledge that the Trust funds were being misused.

In at least three places, the Supreme Court of Texas emphasizes the fact that the Wichita State Bank & Trust Company received none of the fund and took no part in its spoliation. It notes that the petition desclosed no such case. 127 Tex. 407; 93 S. W. (2d) 705. It distinguishes *United States Fidelity & Guaranty Company v. Adoue & Lobit*, 104 Tex. 379; 137 S. W. 648; 138 S. W. 383, a Texas decision relied upon by Judge Taylor in the Royalty Company opinion, on the ground that the *Adoue & Lobit* case involved a payment of part of the funds to the Bank. In stating the precise question to be decided, in the *Quanah A. & P. Ry. Co.* case, the Court says:

"From the above, it is evident that we must an-

swer the following question in order to decide the case:

"If a person negotiates to a bank a bill of exchange payable on its face to the person negotiating it in a Trust capacity, and the purchasing bank, in the very transaction by which it acquires the instrument, passes its proceeds to the individual checking credit of the Trustee on its books, and thereafter allows him to check out such proceeds on his individual checks, and as a result of such transactions the fund is lost to the true owner, is the bank liable for such loss to such true owner?

"The question involves a case where the bank received no part of the funds, and had no actual knowledge that the funds were being checked to persons not entitled to receive them. Also, a case is involved where the bank made no inquiry." (Italics added.)

Justice Critz expresses for the Supreme Court complete satisfaction with its contemporaneous decision in the present case. His language is here quoted:

"We are satisfied with our opinion in the Wichita Royalty Company case as explained by our opinion on rehearing in that case."

The opinion on rehearing in this case reaffirms all principles of law laid down in the original opinion:

"The principal aim of the original opinion is to set forth the principles of law applicable upon another trial." Wichita Royalty Co. v. City National Bank, 127 Tex. 158; 93 S. W. (2d) 143.

The Court wrote another opinion on rehearing, simply to indicate that it had settled the applicable law

without attempting to resolve fact questions appearing on another trial. 127 Tex. 158; 93 S. W. (2d) 143, 144. Hence, the Supreme Court of Texas did what the Circuit Court of Appeals has done in laying down rules of law to govern the facts to be found by the trial Court.

The difference between the two Courts on material legal issues is, in the main, fourfold:

1. The Texas Court's rule of constructive notice after receipt of payment is rejected by the Circuit Court, and in its stead actual knowledge of each wrongful transaction measures the liability.

2. Harrell's liability is limited to funds received with notice and diversions in which he knowingly assisted, whereas the Supreme Court of Texas applied to Harrell the same rule of constructive notice as that applied to the Bank.

3. The Circuit Court held that the Marlborough transaction was unauthorized, but that it might be sustained if the succeeding Trustee accepted a valid title in an effort to save a doubtful obligation of Peckham's estate; whereas, the rule promulgated by the Supreme Court of Texas recognized no circumstance under which the Trust would be bound by this transaction.

4. The Circuit Court held that Peckham's sale as an individual to himself as Trustee was an account of Trust moneys used therefor, because the bank was not a party to these transactions; whereas, the Supreme Court of Texas held that such dual dealings of the Trustee were voidable at the election of his successor, and that the Bank's duty to supervise the commingled account was not

relaxed by reason of its not being a party to these transactions.

The question of limitation, decided in favor of the Trust by the Supreme Court of Texas, is left open by the Circuit Court of Appeals. Other questions ruled by the Supreme Court of Texas, but not expressly passed upon by the Circuit Court of Appeals, were likewise left open.

The Circuit Court of Appeals is right in holding that the Bank was liable for the payments received by it on Peckham's personal indebtedness. It likewise is right in its holding that the Bank is liable for the amounts represented by checks on their face payable to the Bank and credited to the personal account of Peckham. These checks aggregate more than $75,000.00 and primarily concern the Marlborough transaction. The Supreme Court of Texas did not consider this question since its rule of constructive notice would include liability on these items, irrespective of their distinctive character.

Apart from notice given the Bank by participation in the fund, recovery on the checks payable to its order is obviously justified on the reasoning advanced by the Circuit Court. The very form of the checks required that the Bank refuse to pass them to the individual account of the Trustee. *Robbins v. Passaic National Bank*, (N. J. Court of Appeals and Errors) 109 N. J. L. 250, 82 A. L. R. 1368.

The opinion of the Supreme Court of Texas in this case embodies the controlling State law applicable still and controlling the decision in the Federal Courts. In substantial respects, the Circuit Court of Appeals has differed with that decision. The two decisions are hopelessly

irreconcilable. The Circuit Court of Appeals recognized that it was differing from the Supreme Court of Texas upon original hearing. 95 Fed. (2d) 671, 675. After *Erie Ry. Co. v. Tompkins, supra,* and petitioners' asking leave to file and filing a Second Motion for Rehearing, which the Court considered, the Circuit Court professed to follow the Texas law, but based its holding upon the inadequate foundation of a plainly distinguishable State decision contemporaneously rendered.

If the doctrine of *Erie Ry. Co. v. Tompkins, supra,* and *Ruhlin v. New York Life Ins. Co., supra,* is to have any stability and consistency of application, the Federal Courts will not be left free to determine the applicable State law by resort to pure speculation on the future trend of that law. If an established precedent can be so easily displaced, it may as well be said that the Federal Courts will determine the State law in the first instance.

Wherefore, prayer is made that the judgment of the Circuit Court of Appeals for the Fifth Circuit be reversed, and that the law as decided by the Supreme Court of Texas in this case be applied, and for general and special relief.

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APPENDIX

Peckham for the trust borrowed $15,000.00 from the Bank to pay Harrell and one Basham for Stephens Royalty. (R. pp. 885; 481.) He borrowed $25,000.00 to put his trust behind the Marlborough venture. (R. pp. 1104-1105; 885.) Harrell and Peckham negotiated both loans in 1926, in renewal of which, suit was filed. (R. p. 1104.) The Trial Court correctly held that details of these transactions voided the notes sued on. (R. pp. 1922-1930.) He did not find the details. (R. pp. 1922-1930.) They are without dispute;

On January 1, 1926, Harrell and Peckham were good friends. (R. p. 449.) The former was chief executive officer of the Bank and the latter was trustee of Wichita Royalty Company. (R. p. 420.) They owned Marlborough Addition. (R. p. 1275.) They had acquired or were acquiring the Curlee tract. (R. p. 1267.) Prior thereto Peckham had acquired a one-half interest in Stephens royalty, executing notes for the deferred consideration. (R. pp. 1266-1267; 449.)

Harrell pleaded in four places that he and Basham sold Stephens royalty to Wichita Royalty Company. (R. pp. 262-276.) Likewise he testified that he sold it to Wichita Royalty Company. (R. pp. 1268; 1279.) The deed is dated January 1, 1926, and names Wichita Royalty Company as its grantee. (R. pp. 450-451.)

On January 4, 1926, Peckham transferred $5,000.00 from the trust account to his personal account. (R. pp. 480; 1715; 1019; 1051.) Peckham's checks exhausted his private funds on the seventh, leaving the commingled account consisting wholly of transferred funds. (R. p.

1051.) It so remained until January 11, 1926 (R. p. 1051). That day Peckham transferred another $5,000.00 from the trust account to his personal account. (R. pp. 1715; 480.) Meanwhile on January 8, 1926, G. W. Peckham and J. T. Harrell each had issued their respective checks for $2,567.75 in payment for their joint purchase of the Curlee land, $4,749.10 being deposited to the account of W. S. Curlee on January 8, 1926, and $381.40 being deposited to the account of Welch, Richardson and Kemp, brokers in the deal, on January 8, 1926. (R. pp. 481; 1268; 1798; 1799.)

Peckham's $2,567.75 check paid on the eighth, created an overdraft and it remained an overdraft until it was taken up on January 11, 1926, by the transfer of the second $5,000.00 above. (R. p. 582.)

Peckham's check for $2,567.75 was for part of the joint purchase with Harrell of the Curlee land, Peckham's interest in which land being taken in by Harrell and Basham as a part of the consideration for their sale to Wichita Royalty Company at $1,000.00 more than Peckham paid for it. (R. pp. 1293-1294-1295.) Harrell testified that he and Basham took Peckham's interest in for a known profit to Peckham of $1,000.00. (R. pp. 1293-1294-1295.) Harrell not only knew that in the sale to Wichita Royalty Company Peckham was paying a part of the consideration by a conveyance to Harrell and Basham of property personally owned by Peckham, but also that he was putting it in at a known $1,000.00 profit. (R. pp. 1293-1294-1295.)

The next day, January 12, 1926, at a time when Peckham's commingled account consisted wholly of transferred funds, he paid $454.50 as a part of the joint ac-

count with Harrell and others of the Marborough property. (R. pp. 1539; 1654; 582; 1715.)

Four days later, January 16, 1926, Peckham, trustee, executed a note for $15,000.00. (R. p. 1539.) On the same day Peckham issued his check upon the commingled account for $2,201.32 as the first payment to Harrell and Basham of their sale to Wichita Royalty Company. (R. pp. 1539; 1716.) Of the $2,201.32 so paid Harrell and Basham out of the commingled account, $1,362.87 consisted wholly of funds theretofore transferred from the trust account. (R. pp. 1539; 1716.)

Harrell testified that he had asked customers of the bank when they would make an application for loan what they intended to do with the money. "I never asked George Peckham that that I recall. *I might have.* I don't know whether he would have told me or not. Mr. Peckham never refused to answer any question that I asked him about his business. I might have asked him some questions about his business." (R. p. 450.) He further testified that "frequently when loans are made by the bank of $15,000.00 or $25,000.00, the lending banker inquires the purpose for which the proceeds of the loan are going to be used." (R. p. 1295.)

The second day thereafter, January 18, 1926, Wichita Royalty Company received credit for the proceeds of the $15,000.00 loan made January 16, 1926, against which and on January 18, 1926, Peckham transferred to his personal account $15,769.07. (R. pp. 1539; 1716; 582; 482.) His January eighteenth commingled balance of $18,765.87 was constituted wholly of funds theretofore transferred. (R. p. 1716.)

Thereafter and before another deposit to his personal account and at a time when the commingled account consisted wholly of transferred funds, G. W. Peckham on January 25, 1926, issued his check to J. T. Harrell and C. E. Basham for $10,028.00 which check that day was charged against Peckham's commingled account, $5,014.00 being deposited to the respective accounts of Harrell and Basham in the bank. (R. pp. 1539; 1716; 582.) The $5,014.00 so deposited to the personal account of J. T. Harrell was at a time when on January 25th, his personal balance was $219.16 and his personal liability to the bank was $15,574.44. (R. pp. 1539; 582.) That day and with $4,827.71 of the funds transferred from the trust account to Peckham's account, and then to Harrell's account (J. T. Harrell being the banker who negotiated the January 16th loan from which the proceeds were derived), Harrell paid the bank his private debt of $5,006.67, leaving his personal balance at the close of business January 25, 1926, $186.29. (R. pp. 1539; 482; 1090; 1085.) The banker who negotiated the $15,000.00 received $5,014.00 thereof upon its being transferred to Peckham's commingled account, and such banker paid the bank his private debt with $4,827.71 of the proceeds of the $15,000.00 loan. (R. pp. 482; 1539; 1540.)

A week later and on February 2, 1926, G. W. Peckham caused trust check 465 for $400.00 to be issued and deposited to his personal account. (R. pp. 484; 1540.) That same day G. W. Peckham drew his personal check against the commingled account for $5,100.00 payable to the order of J. T. Harrell and C. E. Basham which such bankers cashed and which check was charged against the commingled account at a time when it required $3,074.15

of the moneys theretofore transferred from the Royalty account to Peckham's personal account to pay the $5,100.00 check. (R. pp. 1716; 484.) On February 13, 1926, G. W. Peckham paid the respondent bank $550.00 from his commingled account upon his private debt. (R. pp. 485; 1540; 1716.)

On March 1, 1926, G. W. Peckham owed the respondent bank $28,050.00 with interest. (R. pp. 1082; 1104; 1540; 486.) His beginning balance that day was $341.90. (R. pp. 486; 1105; 1540.) J. T. Harrell then owed the Bank $7,060.00. (R. pp. 486; 1085; 1540.) G. W. Peckham and J. T. Harrell were still jointly obligated upon the Marlborough indebtedness in excess of $50,000.00. (R. pp. 1540; 486.) W. H. Peckham then owed the Bank $6,120.00 and was jointly liable with J. T. Harrell and G. W. Peckham upon the Marlborough indebtedness. (R. pp. 1105; 1098; 1540.)

On March 1, 1926, the plat and dedication of Marlborough Addition had not been filed for record. (R. p. 1287.) The land had been acquired for the purpose of its development as a suburban addition. (R. p. 1275.) It had no actual or prospective value as oil property. At that time the partners were faced with the necessity of expending large sums of money and incurring large items of expense in paving, laying sewer lines, and in other ways developing the property. (R. p. 476.)

G. W. Peckham was greatly involved. (R. pp. 486; 1104.) He had consistently owed the respondent Bank large sums of money for a long period of time. (R. pp. 1080-1081-1082-1083.) Wichita Royalty Company had large holdings of valuable properties, a substantial monthly income, and except for the $15,000.00 item above

described, owed no debts other than current items. W. H. Peckham was indebted to the Bank and so was J. T. Harrell. (R. pp. 486; 1540.) They were three of the Marlborough partners. They had theretofore expended $4,567.93, each as their respective costs to the date for expenses incident to the purchase and development of Marlborough Addition. (R. pp. 448; 1104.) Large sums were needed to develop the partnership venture. (R. p. 1276.) A loan was needed. Very frequently Bankers inquire the purpose of a loan. (R. p. 1295.) He "might have" asked Peckham what he wanted to do with the funds. (R. p. 450). Peckham and Harrell concluded negotiations for a $25,000.00 loan, G. W. Peckham, trustee, becoming the joint maker with himself individually upon a $25,000.00 note to the bank and $25,000.00 being deposited to the credit of the trust. (R. pp. 885; 1104; 1540.) G. W. Peckham was the joint maker of the note, which note was original of the present $22,000.00 note. (R. p. 1308.)

The same day that the loan was made, G. W. Peckham issued his check on the commingled account payable to W. H. Peckham for $11,811.85 for W. H. Peckham's sale to G. W. Peckham of W. H. Peckham's one-fourth interest in the Marlborough venture. (R. pp. 583; 1104; 1105; 1541.) G. W. Peckham's personal balance of $341.90 was insufficient to pay W. H. Peckham's checks until March 9, 1926, on which day G. W. Peckham's personal balance of $225.20 consisting wholly of transferred funds was increased $17,623.70 upon trust check No. 478 drawn on and payable to the bank's order and deposited to the drawing trustee's personal account, the trustee causing trust records to show the purpose of the check to be Wichita Roy-

alty Company's acquiring a one-half interest in the Marlborough partnership property. (R. pp. 583; 1105; 1541; 1729.)

The same day G. W. Peckham drew his check against the commingled account consisting wholly of transferred funds for $5.060.00 payable to the order of J. T. Harrell and Basham, which was paid to such bankers, one of whom had loaned G. W. Peckham, trustee, the $25,000.00, from which account the $17,623.70 was transferred to G. W. Peckham's commingled account to make it sufficient to pay the check which Peckham issued to Harrell and Basham. (R. pp. 1105;-1541; 1729.) Very frequently bankers inquire the purpose of a loan. (R. p. 1295.) He "might have" asked Peckham what he wanted to do with the funds. (R. p. 450.) Peckham and Harrell concluded negotiations for a $25,000.00 loan, G. W. Peckham becoming the joint maker with himself individually upon a $25,000.00 note to the bank and $25,000.00 being deposited to the credit of the trust. (R. pp. 885; 1104; 1540;.) G. W. Peckham was the joint maker of the note, which note was the origin of the present $22,000.00 note. (R. p. 1308.)

On March 9, 1926, W. H. Peckham's $11,811.85 check cleared against the commingled account and same was added to his then deposit balance of $518.52. (P. pp. 1096; 1105; 1729; 1541.) On the same day W. H. Peckham paid the bank his personal indebtedness of $6,120.00, being a payment to the bank of $5,601.48 of the proceeds of the $25,000.00 loan first deposited to the Wichita Royalty Company account, then transferred to G. W. Peckham's account, then transferred to W. H. Peckham's account, and therefrom paid to the bank which loaned the $25,000.00. (R. pp. 1098; 1104-1105; 1541.)

Thereafter on March 31, 1926, G. W. Peckham from his commingled account paid to Harrell and Basham $5,087.00. (R. pp. 1729; 1106.)

The beginning balance of G. W. Peckham on March 31, 1926, was $503.98 which was constituted wholly of trust funds theretofore transferred to the commingled account on March 6, 1926. (R. pp. 1729; 1106; 584.)

To this beginning balance of $503.98 and on March 31, 1926, Peckham caused trust check No. 485 for $7,500.00 to issue, drawn on and payable to the order of the respoondent bank, and which the respondent bank permitted to be deposited to the personal account of G. W. Peckham from which transferred funds, G. W. Peckham paid to J. T. Harrell and C. E. Basham $5,087.00, said payments to said banker being constituted wholly of trust funds theretofore transferred to the trust account. (R. pp. 1729; 1106; 584.)

Up to March 1, 1926, W. H. Peckham and G. W. Peckham jointly had been out on Marlborough Addition $9,047.50. (R. pp. 1542; 1104.) G. W. Peckham had been out $4,523.75. The witness, Lambert, did not know whether Harrell asked Peckham why he wanted to borrow these moneys in 1926. (R. p. 1542.) "Occasionally Bankers ask applicants for loan what they expect to do with the proceeds," Lambert testified. (R. p. 1542.) Harrell testified that very frequently inquiry would be made and that he might have asked Peckham what he intended to do with the proceeds of the loan. (R. p. 1295.) Occasionally Peckham advised with Harrell with reference to his financial affairs. (R. p. 450.)

On April 10, 1926, G. W. Peckham executed the Marl-

borough deed purporting to convey to his trust one-half interest in Marlborough Addition. The deed bears no revenue stamps. It was never recorded. (R. pp. 693, 733, 736-737.) Harrell knew of Bill Peckham's sale about the time he sold. (R. p. 1287.) The deed was handed to the bookkeeper of the trust with instructions not to let anyone see it. (R. pp. 698, 739.) It was delivered with a letter. (R. pp. 785-786.) The letter recites that one-half interest "is held in my name because of the *fact* that the other owners would not care to be associated with a stock company but *are willing* to be partners with *me as an individual*." (R. pp. 785-786.) Italics added.

The stockholders of the trust were never advised of the existence of the deed or of the trust's supposed interest in Marlborough venture. (R. pp. 685, 739, 745.) Peckham dealt with the interest as his own. At the time of Peckham's death, good title stood in the name of Texas Investment Company. (R. p. 1280.)

Check No. 487 for $17,623.70, No. 485 for $7,500.00, No. 503 for $3,000.00, No. 507, for $1,500.00, No. 510 for $4,500.00, No. 519 for $1,000.00, No. 525 for $4,000.00, No. 432 for $4,357.58, No. 516a for $538.16, No. 571 for $2,000.00, and No. 579 for $2,500.00, total $58,019.44, which checks were payable to the order of the bank, were transferred to and deposited in the personal account of G. W. Peckham with the bank and by him misappropriated, the trust books causing items to be entered as in payment of Marlborough Addition. (R. p. 1542.)